

Internal Revenue Service

Number: **200910001**
Release Date: 3/6/2009
Index Number: 7702.00-00

Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
CC:FIP:B04
PLR-117148-08

Date:
September 08, 2008

Taxpayer =

Parent =

Date 1 =

State A =

State B =

Dear :

This is in reply to the Date 1 letter and subsequent letters submitted by your authorized representatives, requesting a ruling regarding the federal income tax treatment under section 7702(e) of the Internal Revenue Code (Code) of individual contracts (Certificates) provided under a group permanent variable life insurance contract (Group Policy) that Taxpayer plans to issue. Taxpayer will issue the Group Policy to large employers or trusts established for such employers (Employers), which will use the coverage provided by the Group Policy to provide life insurance protection as an employee benefit for some or all of their employees (Covered Employees).

FACTS

Taxpayer makes the following representations. Taxpayer is an insurance company subject to taxation under Part I of Subchapter L of the Code. Taxpayer is a stock life insurance company organized and operated under the laws of State A. Taxpayer is licensed to engage in the life insurance business in State B. Taxpayer joins in the filing

of a consolidated federal income tax return with Parent on a calendar year basis, using an accrual method of accounting.

The Group Policy is a private placement group flexible premium variable life insurance policy. Each Certificate issued under the Group Policy will be a variable contract within the meaning of section 817(d) and will be treated as a separate life insurance contract for purposes of section 7702. Each Certificate will be designed to qualify as a life insurance contract for federal income tax purposes by meeting the requirements of the cash value accumulation test of sections 7702(a)(1) and (b) (CVA test).

Taxpayer plans to issue the Group Policy to Employers that will use it to provide life insurance benefits to the Covered Employees. The Employer will establish a plan pursuant to which the Covered Employees will be provided with life insurance protection while they remain employed with the Employer. The coverage provided to each Covered employee will be evidenced by a Certificate and, during his or her term of employment, the Covered Employee will be entitled to name the beneficiary of the Certificate's death benefit.

Each Certificate will provide a death benefit to the named beneficiary upon the insured individual's death (Death Benefit). The Death Benefit will equal the greater of (1) the "Face Amount" of coverage under the Certificate, and (2) the amount obtained by dividing the Certificate's cash value (referred to as the "Contract Fund" allocable to the Certificate) by a net single premium factor that is intended to ensure compliance with the CVA test. In particular, the net single premium factor per \$1 of death benefit is determined (1) on the basis of interest at the greater of an annual effective rate of 4% or the rates guaranteed on issuance of the Group Policy, (2) using mortality charges determined in accordance with the 2001 Commissioners' Standard Ordinary mortality tables (sex distinct), and (3) by taking into account a level death benefit of \$1 that is provided through the insured's age of 100.

If the Covered Employee dies while employed by the Employer, the Covered Employee's beneficiary will receive the Death Benefit payable under the Certificate. Similarly, if the Employer were to continue coverage under a Certificate after the insured terminates his or her employment with the Employer, then the Death Benefit will be payable to the Covered Employee's beneficiary upon the insured's death provided that the Employer has not changed the beneficiary.

The Group Policy provides for the payment of an initial premium and allows for subsequent premiums that are flexible in amount and timing, subject to the Taxpayer's approval. Only the Employer can pay premiums; the Covered Employees cannot. To avoid a lapse of a certificate, the Employer must pay premiums at least sufficient to fund the monthly charges assessed under the Certificate for the cost of the life insurance protection provided thereunder and other expenses.

Prior to the issuance of the Group Policy, the Taxpayer will actuarially calculate the aggregate initial premium payment that it projects the Employer will need to make in order to purchase the desired level of coverage under the Certificates. The Employer will pay that amount to the Taxpayer in a single cash sum and the Taxpayer will allocate that amount among the Certificates as the initial premium for each Certificate. Taxpayer represents that the cost of providing a given amount of life insurance coverage generally is lower for younger individuals than it is for older individuals and thus the amount of the monthly cost of insurance is similarly lower for younger individuals, the initial premium paid for a Certificate will be lower for younger insureds and higher for older insureds.

When a Covered Employee terminates employment with the Employer, the Taxpayer expects the Employer to exchange the Certificate insuring the life of that individual for a new Certificate insuring the life of a different Covered Employee. The Group Policy states that the Employer may seek to do so, but is not obligated to do so. At that time, the Employer may also change the named beneficiary. The Taxpayer plans to advise the Employer that each such exchange will be treated as a taxable exchange governed by section 1001 and Rev. Rul. 90-109, 1990-2 C.B. 191.

Because the proposed arrangement will utilize taxable exchanges of Certificates when Covered Employees terminate employment, the economics of the arrangement are based in part on limiting the amount of premiums paid into each Certificate to an amount that will fund the cost of insurance for the anticipated employment term based on the age of the Covered Employee. As a result, for a Covered employee who was younger or middle-aged when his or her Certificate was issued, the amount of the initial premium payment may be insufficient to generate the cash value needed to continue supporting the cost of insurance charges as the employee becomes older. Accordingly, as a Covered employee ages, additional premium payments generally will be paid into the Certificate covering the life of that individual.

The source of these additional premium payments generally will be derived from other Certificates issued under the Group Policy, rather than additional cash outlays by the Employer. It is anticipated that, when the Covered Employee terminates employment, the Employer will exchange the Certificate covering that individual's life for a new Certificate covering the life of another Covered Employee. In some of those cases, the exchange proceeds might exceed the amount of the initial premium payment for the new Certificate, in which case the excess could be used to pay additional premiums on other Certificates. Alternatively, the Employer could receive funds to use as additional premiums for one Certificate by taking a withdrawal from (or surrendering) another Certificate. As a result, the Employer generally will need to make only a single cash outlay at the inception of the Group Policy to fund its employee benefit obligations fully, and all subsequent premiums required under the arrangement will be generated through taxable exchanges, taxable withdrawals or taxable surrenders. The Employer can request a loan from one or more Certificates to obtain the funds needed to pay

additional premiums on other Certificates. Only the Employer can request a loan using the Certificates as collateral.

The Cash Value and any loan value will belong to the Employer; the individuals who are insured under the Certificates will have no rights to these amounts.

Thus, even though subsequent premium payments will be necessary and will be paid into the Certificates, the arrangement will function much like a paid-up group variable life insurance policy from the perspective of the Employer because it generally will require the Employer to make only a single cash outlay at inception.

REQUESTED RULING

Whether, pursuant to section 7702(e)(1)(B) and (C), the net single premium within the meaning of section 7702(b) will be determined for each Certificate by assuming that the Face Amount of the Certificate is provided until age 100 of the insured thereunder.

LAW AND ANALYSIS

Section 7702(a) of the Code provides that, for a contract to qualify as a life insurance contract for Federal income tax purposes, the contract must be a life insurance contract under the applicable law and must either (1) satisfy the cash value accumulation test of section 7702(b), or (2) both meet the guideline premium requirements of section 7702(c) and fall within the cash value corridor of section 7702(d). A contract meets the cash value accumulation test of section 7702(b) if, by the terms of the contract, the cash surrender value of the contract may not at any time exceed the net single premium that would have to be paid at that time to fund future benefits under the contract.

To meet the cash value accumulation test of section 7702(a)(1) and (b), the "cash surrender value" (as defined in section 7702(f)(2)) of a contract at any time cannot, by the contract's own terms, be capable of exceeding the "net single premium" that would have to be paid at that time for the "future benefits" under the contract. Section 7702(b) requires that the "net single premium" be computed using: (1) an interest rate, which is the greater of an annual effective rate of 4% or the rate or rates "guaranteed" on issuance of the contract; (2) reasonable mortality charges that (except as provided in regulations) do not exceed the mortality charges specified in the prevailing commissioners' standard tables (as defined in section 807(d)(5)); and (3) in the case of "qualified additional benefits", any reasonable charges (other than mortality charges) for "qualified additional benefits" to the extent that those charges are reasonably expected to be actually paid. "Cash surrender value" is defined as the "cash value" (that is, the amount to which a policyholder is entitled upon surrender of the contract and/or against which the policyholder can borrow) of a contract without regard to any surrender charge, policy loan, or reasonable termination dividend.

Section 7702(e) provides computational rules applicable to the determination of the amount of "future benefits" taken into account in calculating the "net single premium". Specifically, section 7702(e)(1) provides, for purposes other than the cash value/minimum risk corridor test under section 7702(d), that --

(A) the death benefit (and any qualified additional benefit) shall be deemed not to increase,

(B) the maturity date, including the date on which any benefit described in subparagraph (C) is payable, shall be deemed to be no earlier than the day on which the insured attains age 95, and no later than the day on which the insured attains age 100,

(C) the death benefits shall be deemed to be provided until the maturity date determined taking into account subparagraph (B), and

(D) the amount of any endowment benefit (or sum of endowment benefits, including any cash surrender value on the maturity date determined by taking into account subparagraph (B) shall be deemed not to exceed the least amount payable as a death benefit at any time under the contract.

Taxpayer has represented that each Certificate issued under the group policy will be designed to qualify as a life insurance contract for federal income tax purposes by meeting the requirements of the cash value accumulation test of sections 7702(a)(1) and (b) (CVA test). Accordingly, pursuant to section 7702(e)(1)(B) and (C), the net single premium within the meaning of section 7702(b) will be determined for each Certificate by assuming that the Face Amount of the Certificate is provided until age 100 of the insured thereunder.

Except as set forth above, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter, or concerning the manner in which the use of the 2001 CSO tables described in Notice 2006-05 will affect the determination of net single premiums for the Certificates, including whether or how such net single premium might or might not reflect the fact that the 2001 CSO tables extend to age 121.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representatives.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by

PLR-117148-08

attaching a statement to their return that provides the date and control number of the letter ruling.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

/S/

DONALD J. DREES, JR.
Senior Technician Reviewer, Branch 4
Office of the Associate Chief Counsel
(Financial Institutions & Products)